

***United States Court of Appeals
for the Second Circuit***



APPENDIX

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Signed
74-2434

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

HICKS NURSERIES, INC.,

Appellee

v.

COMMISSIONER OF INTERNAL REVENUE,

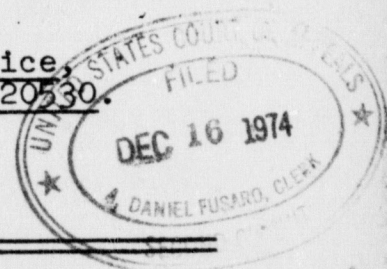
Appellant

ON APPEAL FROM THE DECISION OF
THE UNITED STATES TAX COURT

APPENDIX

SCOTT P. CRAMPTON,
Assistant Attorney General,

GILBERT E. ANDREWS,
ARTHUR L. BAILEY,
Attorneys,
Tax Division,
Department of Justice,
Washington, D.C. 20530.

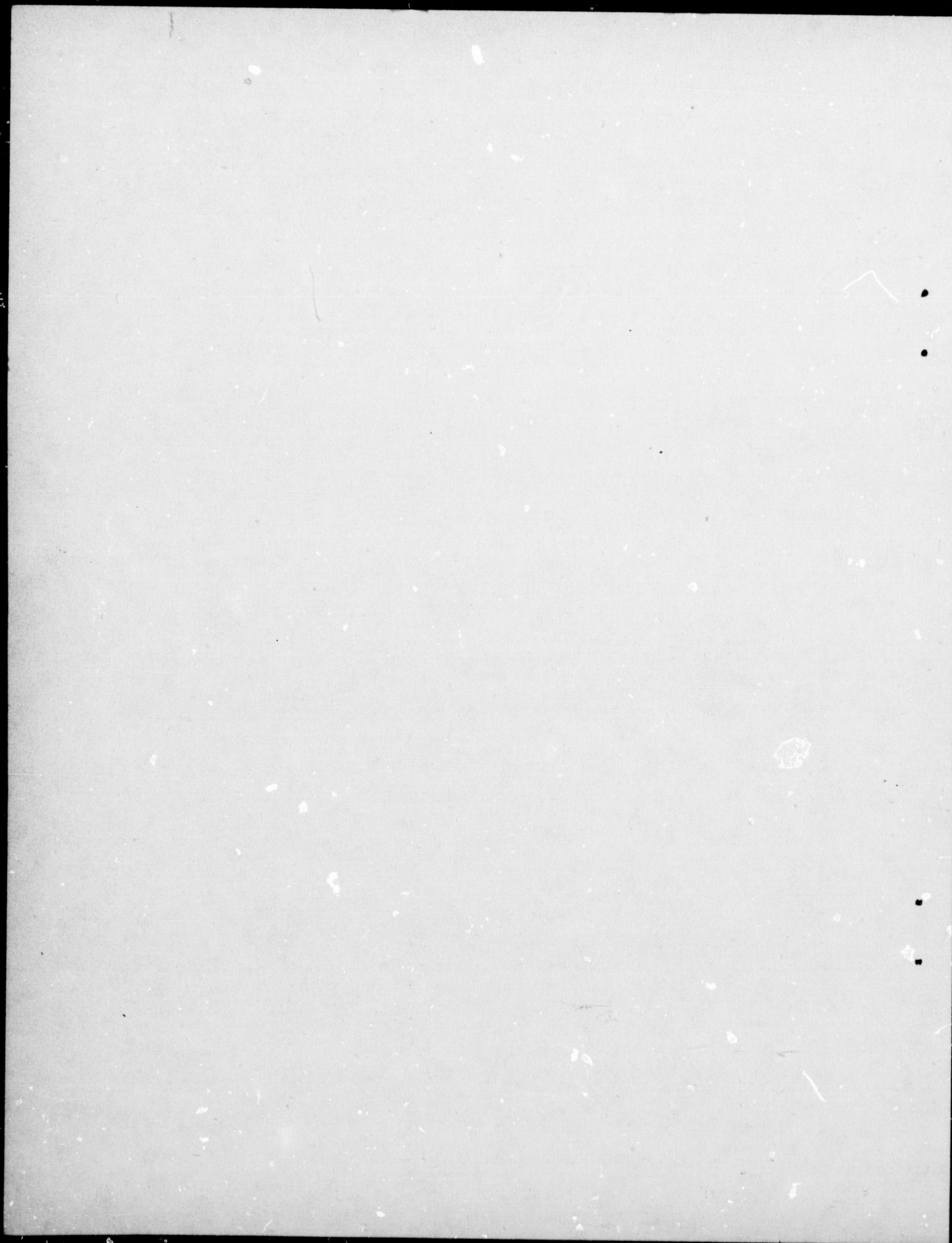


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TAX COURT OF THE UNITED STATES GENERAL DOCKET

DOCKET NO. 1513-70

HICKS NURSERIES, INC.
(Edwin W. Hicks, Treasurer)
100 Jericho Turnpike,
Westbury, N.Y. 11590

PETITIONER.

VS.

COMMISSIONER OF INTERNAL REVENUE.

RESPONDENT.

APPEARANCES FOR PETITIONER:

NAME Robert Anthoine, (Winthrop, Stinson, Petros
and Roberts), 40 Wall Street,
New York, N.Y. 10005
ADDRESS Glenn E. Coven, Jr., (1/15/73, same add.)

Date Month Day Year	Filings and Proceedings	Action	Served
Mar. 13, 1970	PETITION FILED: FEE PAID Mar. 13, 1970		Mar. 24, 1970
Mar. 13, 1970	REQUEST by petr. for trial at New York, N.Y.	GRANTED Mar. 24, 1970	Mar. 24, 1970
May 13, 1970	ANSWER filed by RESP.		May 14, 1970
Dec. 27, 1971	NOTICE OF TRIAL on Mar. 20, 1972 at New York, N.Y.		Dec. 27, 1971
Mar. 20, 1972	HEARING at New York, N.Y. before Judge Goffe.		
	Continued Generally. See Order.		
Mar. 20, 1972	ORDERED, this case continued generally.		Mar. 27, 1972
Apr. 17, 1972	TRANSCRIPT of Mar. 20, 1972 rec'd.		
Sept. 28, 1972	MOTION by Petr. to set this case for trial on March 19, 1973, at New York, N.Y. (No Obj. Resp.)	GRANTED Sept. 29, 1972	Oct. 3, 1972
Jan. 10, 1973	NOTICE for Trial at New York, N.Y. on March 19, 1973		Jan. 10, 1973
Jan. 12, 1973	ENTRY OF APPEARANCE by Glenn E. Coven, Jr. as counsel for petr. filed.		Jan. 26, 1973
Jan. 25, 1973	MOTION by Petr. to strike or a further and better statement,		
Jan. 29, 1973	MOTION by Petr. for leave to file Motion to Strike etc. GRANTED.		
Jan. 31, 1973	MOTION by Petr. to strike or, alternatively, for a further and better statement filed.	Jan. 31, 1973 Feb. 13, 1973	Jan. 31, 1973
Jan. 31, 1973	NOTICE of hearing on Petr's motion filed Jan. 31, 1973, at Washington, D.C. on Feb. 14, 1973.		Jan. 31, 1973
Feb. 9, 1973	NOTICE OF NO OBJECTION to Petr's Motion, filed by Resp.		Feb. 13, 1973
Feb. 9, 1973	AMENDMENT TO ANSWER filed by Resp.		Feb. 13, 1973

CONTINUED ON PAGE 2.

Form No. 10
March 1969

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DOCKET NO. 1511-70

(Continued)

HICKS NURSERIES, INC.			PETITIONER	PAGE 2
Date	Filings and Proceedings	SIMPSON	Action	Served
Month Day Year				
Feb. 13, 1973	ORDER, that Petr's motion filed Jan. 31, 1973 is denied, and further,			Feb. 13 1973
	ORDER, that this case is hereby stricken from			
	Feb. 14, 1973 at Wash. D.C.			
Feb. 23, 1973	REPLY to amended answer filed by petr.			Feb. 26, 1973
March 19, 1973	TRIAL at New York, N.Y. before Judge Simpson.			
	STIPULATION OF FACTS with Exh. filed.			
	PETR. BRIEF DUE - May 13, 1973.			
	RESP. BRIEF DUE - July 17, 1973.			
	PETR. REPLY BRIEF DUE - Aug. 10, 1973.			
	SUBMITTED TO JUDGE SIMPSON.			
April 5, 1973	TRANSCRIPT of Mar. 19, 1973 rec'd.			
May 3, 1973	BRIEF for Petitioner filed.			May 4, 1973
July 16, 1973	MOTION by Resp. to extend time to July 31, 1973 within	GRANTED		JUL 18 1973
	which to file brief in answer.			
July 31, 1973	BRIEF IN ANSWER for Resp. filed.			AUG 1 1973
Aug. 29, 1973	REPLY BRIEF for Petr. filed..			AUG 29 1973
May 6, 1974	OPINION filed, Judge Simpson			MAY 6 1974
	Decision will be entered for the Petr.			
May 6, 1974	DECISION entered, Judge Simpson.			MAY 6 1974
	APPELLATE PROCEEDINGS			
AUG. 2, 1974	NOTICE OF APPEAL to U.S.C.A., 2nd Cir., filed by Resp.			AUG. 5, 1974
AUG. 5, 1974	NOTICE of Filing with copy of notice of appeal sent to			
	Mr. Robert Anthoine, counsel for Petr.			AUG. 5, 1974
AUG. 5, 1974	NOTICE, to parties, of assembling and date for transmission of the record.			AUG. 5, 1974

(continued on page 3)

UNITED STATES TAX COURT
GENERAL DOCKET

DOCKET NO. 1513-70

(Continued)

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UNITED STATES TAX COURT

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HICKS NURSERIES, INC., :

Petitioner, :

v. :

Docket No.: 1513-70

COMMISSIONER OF INTERNAL REVENUE, : [Filed March 19, 1973]

Respondent. :

- - - - - x

STIPULATION OF FACTS

The parties hereby stipulate and agree that for the purpose of this case the following facts and exhibits attached hereto and made a part hereof may be taken as true, subject to the rights of the parties to introduce other and further evidence not inconsistent with this stipulation and preserving the parties' rights to object, at the time of trial, to any and all portions of said stipulation and attached exhibits as they may deem to be irrelevant or immaterial.

1. The Petitioner is Hicks Nurseries, Inc., a New York corporation the principal office of which at the time of filing the petition herein was located at 100

- 5 -

Jericho Turnpike, Westbury, New York. For the years 1964 through 1967, the Petitioner filed its U.S. Small Business Corporation Return of Income on Forms 1120-S with the District Director of Internal Revenue, Brooklyn, New York. Copies of these returns are attached as Exhibits 1-A, 2-B, 3-C and 4-D.

2. The Petitioner was organized in 1932 to succeed to the wholesale and retail nursery and landscaping business that had been conducted by the Hicks family since approximately 1853. All of the stock of the Petitioner is presently, and always has been, owned by members of the Hicks family or persons related to them and by certain employees.

3. As of January 1, 1964, all of the outstanding stock of the Petitioner was owned as follows:

Edwin W. Hicks	412
Eloise L. Hicks	42
Mr. & Mrs. Hicks, jointly	2
Alfred H. Hicks	49
Susan L. Hicks	20
Ralph Hicks	25
John M. G. Emory	16
Esther H. Emory	46
Mr. & Mrs. Emory, jointly	2
Margaret W. Emory	12
Edwin H. Costich	31
Peter E. Costich	25
Robert J. Patterson	12
Earl M. Good	17
Total	711

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4. During the year 1963, the Petitioner had 17 shareholders. In an effort to meet the requirements of § 1371(a)(1) of the Internal Revenue Code, 5 shareholders were eliminated by redemptions of their shares, and 4 shareholders consisting of two married couples who held all of their shares in their individual names each transferred one share into a joint tenancy with his spouse. Thus, prior to December 31, 1963, Edwin W. Hicks owned 413 shares and his wife Eloise owned 43. On that day, Edwin and Eloise each transferred one share into their joint names so that thereafter Edwin owned 412 shares, his wife owned 42 shares and two shares were registered in their joint names. Similarly, Edwin's sister, Esther Emory and her husband, John M. G. Emory, each placed one share in their joint names so that on December 31, 1963, John owned 16 shares, Esther owned 46 shares and two shares were registered in their joint names.

5. On January 30, 1964, the Petitioner filed an Election by a Small Business Corporation on Form 2553 with the District Director, Brooklyn, New York. A copy of such election is attached as Exhibit 5-E.

[-4-]

6. On March 6, 1966 John M. G. Emory, a shareholder of Petitioner, died. Letters testamentary were issued to his wife, Esther H. Emory, on April 5, 1966.

7. Esther H. Emory, as Executrix, did not file a consent to Petitioner's election to be taxed as a small business corporation within 30 days of her qualification as executrix.

8. Esther Emory's failure to file a consent as executrix of her husband's estate was first called to the attention of petitioner's counsel in January 1972.

9. By letter dated July 5, 1972, addressed to the District Director of Internal Revenue, Brooklyn, New York, Petitioner and Esther H. Emory, as Executrix of the Estate of John M. G. Emory, requested an extension of time under § 1.1372-3(c) of the Income Tax Regulations, to file a consent to the Petitioner's election to be taxed as a "small business corporation." A copy of this letter is attached as Exhibit 6-F. Respondent stipulates this letter for the sole purpose of showing that an extension of time was requested and not for the truth of the matters stated therein.

[-5-]

10. By letter dated September 18, 1972, the Director of the Internal Revenue Service Center, Holtsville, New York, granted an extension of time until October 18, 1972, to file a consent. A copy of this letter is attached as Exhibit 7-G.

11. By letter dated September 25, 1972, the Director of the Internal Revenue Service Center, Holtsville, New York, stated that the grant of the extension of time was revoked. A copy of this letter is attached as Exhibit 8-H.

12. By letter dated September 27, 1972, there was mailed to and received by the Internal Revenue Service Center, Holtsville, New York, a consent of Esther H. Emory, Executrix. Such consent was accompanied by the consents of all other persons who owned stock in the Petitioner between January 1, 1966 and September 18, 1972. Copies of said letter and consents are attached as Exhibit 9-I.

13. By letter dated October 20, 1972, the acting Director of the Internal Revenue Service Center, Bohemia, New York, stated that the request for an extension of time

[-6-]

in which to file the consent of Esther H. Emory, Executrix, was denied. A copy of this letter is attached as Exhibit 10-J.

14. Attached hereto are copies of the following letters:

<u>From</u>	<u>To</u>	<u>Date</u>	<u>Ex. No.</u>
Frederick Hackett	District Director	9-13-72	11-K
Frederick Hackett	District Director	10-2-72	12-L
District Director	Hicks Nurseries c/o Frederick Hackett	10-4-72	13-M
Frederick Hackett	District Director	10-30-72	14-N
District Director	Frederick Hackett	11-15-72	15-O
Frederick Hackett	District Director	11-21-72	16-P
District Director	Frederick Hackett	12-4-72	17-Q
Frederick Hackett	District Director	12-12-72	18-R

/s/ Robert Anthoine
Counsel for Petitioner.

(Sgd) LEE H. HENKEL, JR. - JJM

LEE H. HENKEL, JR.,
Chief Counsel,
Internal Revenue Service.

FORM 2553 (REV. MAR. 1962) U. S. TREASURY DEPARTMENT INTERNAL REVENUE SERVICE	ELECTION BY SMALL BUSINESS CORPORATION As to taxable status under subchapter S of the Internal Revenue Code
---	--

NOTE: This election under section 1372(a) (with the consent of all your stockholders) to be treated as a "small business corporation" for income tax purposes may be made only if the corporation is a domestic corporation which is not a member of an affiliated group (as defined in section 1504) and which has (1) no more than 10 shareholders; (2) only shareholders (other than an estate) who are individuals; (3) no shareholder who is a nonresident alien; and (4) only one class of stock.

Name of corporation HICKS NURSERIES, INC.	Employer identification number 11-1383568
---	---

Number and street 100 JERICHO TURNPIKE, WESTBURY, N.Y.	
--	--

City or town, postal zone number, county, State WESTBURY, NASSAU COUNTY, N.Y.	Date submitted JAN 29, 1964
---	---------------------------------------

Election is to be effective for the taxable year beginning Mo. Jan , Yr. 64	Place incorporated New York	Date incorporated December 1932	Number of shares issued and outstanding 211
--	---------------------------------------	---	---

Is the corporation the outgrowth or continuation of any form of predecessor? <input checked="" type="checkbox"/> YES <input type="checkbox"/> NO	If "Yes", state name of predecessor, type of organization, and the period during which it was in existence Isaac Hicks and Sons - partnership aprox 1865 to 1932
---	--

Principal business activity (see instruction 1)
Agricultural nursery - growing of plants, trees and shrubs and sales of same

Name and address of each shareholder	Number of shares	Internal Revenue District where individual return is filed
1. Edwin W. Hicks and Eloise L. Hicks 61 Drexel Ave. Westbury, N. Y. NY	H 412 W 42 J 2	First N. Y.
2. Alfred H. Hicks 61 Drexel Ave., Westbury, N. Y.	49	"
3. Susan L. Hicks 61 Drexel Ave. Westbury, N. Y.	20	"
4. Ralph Hicks Jericho Turnpike, Westbury, N. Y.	25	"
5. John M. G. Emory and Esther H. Emory 810 Baldwin Drive, Westbury, N. Y. NY	H 16 W 46 J 2	"
6. Margaret W. Emory, 810 Baldwin Drive Westbury, N. Y.	12	"
7. Edwin H. Costich, 202 Linden Ave., Westbury, N. Y.	31	"
8. Peter E. Costich, Hicks Lane, Westbury, NY	25	
9. Robert J. Patterson, Jericho Turnpike Westbury, N. Y.	12	
10. Earl M. Good, RFD Straight Path Huntington, N. Y.	17	

NOTE: In order for this election to be valid, the consent of each stockholder must be submitted with this form. See instruction 1.

SIGNATURE AND VERIFICATION

I declare under penalties of perjury that this election is duly authorized, and that the statements made herein are to the best of my knowledge and belief true, correct, and complete statements.

Jan 30, 1964

[Signature]

[Signature]

RI NO. **1513-70**
5-E

The purpose of this election is to permit the taxable income of a "small business corporation", to the extent that it exceeds dividends distributed in money out of earnings and profits of the taxable year, to be taxed directly to the shareholders (rather than to the corporation) to the extent that it would have constituted a dividend if it had been distributed on the last day of the corporation's taxable year.

INSTRUCTIONS

A. Corporations eligible to elect.—The election may be made only if the corporation is a domestic corporation; is not a member of an affiliated group of corporations as defined in section 1504 of the Code; and which has (1) no more than 10 shareholders; (2) only shareholders (other than an estate) who are individuals; (3) no shareholder who is a nonresident alien; and (4) only one class of stock.

B. Valid election.—This election shall be valid only if all persons who are shareholders of the corporation on the first day of the corporation's taxable year or on the day of election, whichever is later, consent to such election.

C. Time of making election.—This form must be completed and filed for any taxable year during (a) the first month of such taxable year, or (b) the month preceding such first month. The election shall be effective for the taxable year for which it is made and for all succeeding taxable years unless it is terminated under section 1372(e).

D. Shareholders' statement of consent.—(1) In general.—The consents to the election of the corporation by all shareholders at the date of election (which may be incorporated in one statement) shall be attached to this form. If the election is made before the first day of the corporation's taxable year, the consents of persons who became shareholders after the date of the election and on or before such first day shall be filed with the district director with whom this election was filed as soon as practicable after such first day but in no event later than the last day prescribed for filing the election. The statement shall set forth the name and address of the corporation and of each shareholder, the number of shares of stock owned by each shareholder, and the date(s) on which such stock was acquired. The consent of a minor shall be made by the minor or by his legal guardian, or his natural guardian if no legal guardian has been appointed. The consent of an estate shall be made by the executor or administrator thereof.

(2) New shareholders.—If a person becomes a shareholder after the first day of the taxable year for which the election is effective, or after the day on which the election is made (if such day is later than the first day of the taxable year), the consent of such shareholder shall be made in a statement filed (with the district director with whom the election is filed) within the period of 30 days beginning with the day on which such person becomes a new shareholder. If the new shareholder is an estate, the 30-day period shall not begin until the executor or administrator has qualified under local law to perform his duties, but in no event shall such period begin later than 30 days following the close of the corporation's taxable year in which the estate became a shareholder. The statement of consent shall set forth the name and address of the corporation and of such new shareholder, the number of shares of stock owned by such shareholder, the date on which such shares were acquired, and the name and address of each person from whom such shares were acquired. Note: Failure of a new shareholder to consent to the election within this required period terminates the election.

E. Principal business activity.—In reporting the principal business activity give the one business activity that accounts for the largest percentage of "total receipts". "Total receipts" means gross sales and/or gross receipts, plus all other income. State the broad field of business activity as well as the specific product or service, such as "Mining copper", "Manufacturing cotton broad woven fabric", "Wholesale food", or "Retail apparel".

F. Where to file.—This election is to be filed with the District Director of Internal Revenue for the district in which the corporation's principal place of business or principal office or agency is located.

G. Signature and verification.—This form must be signed either by the president, vice-president, treasurer, assistant treasurer or chief accounting officer, or other corporate officer (such as tax officer) who is authorized to sign.



HICKS=NURSERIES, Inc.=

100

JERICO TURNPIKE

Telephone EDgewood 4-0066

WESTBURY, LONG ISLAND, N.Y.

January 20, 1964

STOCKHOLDERS STATEMENT OF CONSENT TO THE CORPORATION'S ELECTION OF THE TAXABLE STATUS OF A SMALL BUSINESS CORPORATION UNDER SUBCHAPTER 5 OF THE INTERNAL REVENUE CODE - ATTACHED TO FORM 2553

We, the undersigned, representing 100% of the issued and outstanding Capital of Hicks Nurseries, Inc. having attached hereto a historical statement of the position and disposition of the shares of the said corporation, severally consent to the election by Hicks Nurseries, Inc., of the status of a small business corporation under subchapter 5 of the internal revenue code.

NAME AND ADDRESS OF STOCKHOLDER

shares

Edwin W. Hicks	412	husband
Eloise L. Hicks, wife	42	wife
	2	joint

Alfred H. Hicks	49
-----------------	----

Susan L. Hicks	20
----------------	----

The above reside at 61 Drexel ave., Westbury, N. Y.

Ralph Hicks	25
Jericho Turnpike, Westbury, N. Y.	

John M. G. Emory	16	husband
Esther H. Emory, wife	46	wife
810 Baldwin Drive, Westbury, N. Y.	2	joint

Margaret W. Emory	12
810 Baldwin Drive, Westbury, N. Y.	

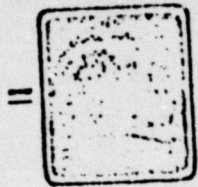
Edwin H. Costich	31
309 Linden Ave., Westbury, N. Y.	

Peter F. Costich	25
Hicks Lane, Westbury, N. Y.	

Robert J. Patterson	12
Jericho Turnpike, Westbury, N. Y.	

Earl M. Good	17
RFD Straight Path, Huntington, N. Y.	

All shares here listed were acquired by inheritance or gift



phone EDgewood 4-0066

HICKS-NURSERIES, Inc.

JERICHO TURNPIKE
WESTBURY, LONG ISLAND, N.Y.

Hicks Nurseries, Inc. 100 Jericho Turnpike, Westbury, N. Y.

Historical Tabulation of acquisition and disposition of Capital Stock
by present stockholders attached to form 2553
December 31, 1963 and January 20, 1964

Dates; Stockholders - see names below

	(1a)	(1b)	(1c)	(2)	(3)	(4)	(5a)	(5b)	(5c)	(6)	(7)	(8)	(9)	(10)
1933	25													
1934	50													
1935	50													
1945	80													
1946	80													
1948	12													
1949	24													
1950	10													
1951	10													
1952	110	12		12		12	12	12	12	12	12	12	12	12
1953	13	13		6		6	5	5	5		5	5		5
1954	6	6		6		6								
1955	4	4		2		2					7	4		
1957	26	4		7		4					7	4		
1959	20	4		7		4		30						
1961	6			6										
1962	6			6										
1963	4	1	2	3			1	1	2					
Total	412	42	2	49	20	25	16	46	2	12	31	25	12	17

Stockholders listed above

~~(1a)~~ Edwin W. Hicks

~~(1b)~~ Eloise L. Hicks

~~(1c)~~ Edwin W. Hicks and Eloise L. Hicks - Joint

(2) Alfred H. Hicks

(3) Susan L. Hicks

(4) Ralph Hicks

~~(5a)~~ John M. G. Emory

(5b) Esther H. Emory

(5c) John M. G. Emory and Esther H. Emory - Joint

(6) Margaret W. Emory

(7) Edwin H. Costich

(8) Peter E. Costich

(9) Robert J. Patterson

(10) Earl M. Good

62 T. C. No. 16

UNITED STATES TAX COURT

HICKS NURSERY, INC., Petitioner v. COMMISSIONER
OF INTERNAL REVENUE, Respondent

Docket No. 1513-70.

Filed May 6, 1974.

The shareholders of a corporation wished to have the corporation elect under sec. 1372, I.R.C. 1954, to be treated as a small business corporation. In order to meet the 10-shareholder requirement of sec. 1371, I.R.C. 1954, H and W, who each owned stock individually, each transferred one share of the stock into joint ownership with the other spouse. Held, in accordance with sec. 1.1371-1(d)(2), Income Tax Regs., H and W are treated as a single shareholder. Held further, merely because the validity of the election was being litigated before the Tax Court was not an adequate reason for the respondent to revoke his grant of an extension of time for filing a consent to an election, and the consent so filed is effective.

SERVED MAY 6 1974

[- 2 -]

Robert Anthoine and Glenn E. Coven, Jr., for the
petitioner.

Agatha L. Vorsanger, for the respondent.

OPINION

SIMPSON, Judge: The respondent determined the following deficiencies in the petitioner's Federal income taxes:

<u>Taxable Year</u>	<u>Deficiency</u>
1964	\$39,761.11
1965	60,739.36
1966	91,514.67
1967	61,319.15

The main issue which we must decide is whether a husband and wife, who each owned stock in a corporation individually and who owned other stock in the corporation jointly, are to be treated as 1 or 2 shareholders for purposes of the 10-shareholder requirement of section 1371¹ (a) (1) of the Internal Revenue Code of 1954. If we decide that the election was valid, then we must decide the subsidiary issue of whether the respondent had adequate grounds for revoking his authorization allowing a new shareholder to file a consent after the expiration of the ordinary period for filing such consent.

1

All statutory references are to the Internal Revenue Code of 1954.

All of the facts have been stipulated, and those facts are so found.

The petitioner, Hicks Nurseries, Inc. (Hicks), was a New York corporation with its principal office in Westbury, New York, at the time of filing its petition herein. For the years 1964 through 1967, it filed its Federal income tax returns with the district director of internal revenue, Brooklyn, New York.

Hicks operated a landscaping and nursery business since its inception in 1853. It was incorporated in 1932; since then, and at least extending to the date of the trial in this case, all of its stock has been owned by the Hicks family, persons related to them, and certain employees. In 1963, the shareholders of Hicks decided that they wished to have the corporation taxed as a small business corporation in 1964. To qualify for such treatment, the number of its shareholders had to be reduced. Some shareholders had their stock redeemed, leaving 12 shareholders prior to December 31 of 1963. Four of the 12 remaining shareholders included two married couples, Edwin and Eloise Hicks and John and Esther Emory. Prior to that date, all their shares were held in their individual capacities; Edwin Hicks owned 413 shares, Eloise Hicks owned 43 shares, John Emory owned 17 shares, and

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Esther Emory owned 47 shares, of a total of 711 shares outstanding. On December 31, 1963, each husband and wife transferred 1 share into a joint tenancy with his other spouse.

On January 30, 1964, Hicks filed its election to be taxed as a small business corporation with the district director of internal revenue, Brooklyn, New York. The election contained the information that Edwin and Eloise Hicks and John and Esther Emory held shares individually as well as jointly. The attached shareholder consents also reflected their ownership pattern. For the years 1964 through 1967, Hicks treated itself as a small business corporation and filed its Federal income tax returns accordingly. The individual and joint ownership of both the Hicks and the Emorys was shown on the returns for the years 1964 and 1965, and for the years 1966 and 1967, the Hicks' joint ownership was shown.

During the years 1964 through 1967, the shareholders of Hicks and their holdings remained basically stable. In 1966, Mr. Emory died, and Mrs. Emory acquired his shares and the shares they had held jointly. In 1967, 2 shareholders' interests were terminated, and 2 other shareholders were married and thereafter held some shares in joint tenancy with their respective spouses.

[- 5 -]

Mr. Emory died on March 6, 1966, and Mrs. Emory was issued letters testamentary on April 5, 1966. As executrix of the estate, she did not file the estate's new shareholder consent to Hicks' election within 30 days of her qualification as executrix. Mrs. Emory did not attempt to file the requisite consent until 1972. Hicks' counsel first learned of her failure to file the consent in January 1972. By a letter dated July 5, 1972, Hicks and Mrs. Emory requested from the district director of internal revenue, Brooklyn, New York, an extension of time in which to file the consent. Since there had been no action on the requested extension and since Hicks' counsel believed that it was necessary to resolve the consent question prior to the litigation over the validity of the election, on September 13, 1972, he wrote a letter to the director of the internal revenue service center in New York State requesting that the director act on the request for an extension. By a letter dated September 18, 1972, the director granted the request for an extension of time and allowed Mrs. Emory until October 18, 1972, to file the consent. However, on September 25, 1972, he wrote to Hicks revoking the extension because further study was needed to determine whether granting an extension would be proper. By a letter dated September 27, 1972, Hicks'

[- 6. -]

counsel forwarded to the director Mrs. Emory's consent and similar consents for all the other people who had owned stock in Hicks between January 1, 1966, and September 18, 1972. All of the shareholders' signatures were dated September 21, 23, or 24, 1972. Hicks' counsel responded to the revocation by writing a letter on October 2, 1972, requesting that the director review and rescind his decision. The acting director wrote a letter on October 20, 1972, to Hicks' counsel, reaffirming the revocation and explicitly denying an extension. Ten days later, Hicks' counsel wrote again to the acting director, protesting his decision and asking for a reconsideration of the request. In a letter dated November 15, 1972, the acting director stated that when the extension was granted, the service center was unaware of the determination that the election was invalid. He revealed that according to the Internal Revenue Service instructions, an extension can be granted only if there is then in effect a valid election and that as soon as the service center became aware of the determination that the election was invalid, the service center revoked the extension. However, Hicks' letters of July 5, 1972, and September 13, 1972, contained the information that the validity of the original election

[- 7. -]

was being litigated in a case currently before the Tax Court.

For the years 1964 through 1967, the petitioner filed small business corporation Federal income tax returns and did not pay any Federal income taxes. In his deficiency notice, the respondent determined that Hicks did not qualify as a small business corporation and was subject to the Federal income taxes imposed by section 11 for all 4 years. The respondent further determined in his amended answer to Hicks' petition that a new shareholder's consent to Hicks' election had not been filed within the applicable period and that for such additional reason, Hicks did not qualify as a small business corporation for the years 1966 and 1967. In its reply, the petitioner alleged that the required consent was properly filed during an extension of time which the respondent had granted but had subsequently improperly revoked.

We must first decide whether the election made by Hicks in 1964 to be taxed as a small business corporation was valid. The answer turns on whether in the circumstances of this case, Mr. and Mrs. Hicks and Mr. and Mrs. Emory are to be considered 2 or 4 shareholders, for purposes of determining the number of shareholders of Hicks.

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Section 1372(a) provides that "any small business corporation may elect * * * not to be subject to the taxes imposed by this chapter." Section 1371(a) defines "small business corporation"; subsection (a)(1) contains the requirement that such a corporation cannot have more than 10 shareholders. Section 1371(c) states, in part, that:

For purposes of subsection (a)(1) stock which--

* * * * *

(2) is held by a husband and wife as joint tenants * * *

shall be treated as owned by one shareholder.

Section 1.1371-1(d)(2)(i), Income Tax Regulations, states, in part:

* * * stock which--

* * * * *

(b) is held by a husband and wife as joint tenants * * *

shall be treated as owned by one shareholder. For this purpose, if a husband or wife owns stock in a corporation individually, and the husband and wife own other stock in the corporation jointly, the husband and wife will be considered one shareholder. However, if the husband and wife each owns stock in the corporation individually, they will be treated as two shareholders. * * *

The petitioner relies upon the second sentence of the regulations and contends that such sentence applies to a situation in which both spouses own stock individually, as

well as when only one spouse owns stock individually. It argues that the "or" in the phrase "husband or wife" includes "and" when not inconsistent with the purposes of the provision. Sec. 1.368-2(h), Income Tax Regs. It recognizes that the words of section 1371(c) apply only to the stock owned by the spouses jointly. In developing the regulations, the I.R.S. recognized that there was a question as to the applicable rule when one spouse owned stock individually and other stock was owned by the spouses jointly. The regulations took the position that in such a situation, the spouses should be treated as a single shareholder. The petitioner suggests that there is no reason for drawing a distinction between that situation and the one in which both of the spouses also own stock individually. It asserts that the third sentence of the regulations applies only when the spouses own no stock jointly and therefore that sentence is not inconsistent with its suggested interpretation of the second sentence.

The respondent urges a different interpretation of the regulations. He contends that the second sentence only applies when one of the spouses owns stock individually. He takes the position that if both of the spouses own stock individually, the third sentence of the regulations is applicable.

In our opinion, the petitioner and its shareholders acted reasonably in adopting their interpretation of the regulations. Hicks had too many shareholders for it to qualify as a small business corporation, and the shareholders had to make some arrangement to reduce their number. Their reading of the regulations was certainly not unreasonable. Although the second sentence literally covered only a situation in which the spouses owned some stock jointly and one spouse owned stock individually, "or" is often used in the regulations when "and/or" is intended. Sec. 1.368-2(h); Income Tax Regs. An attempt to resolve the uncertainty by an examination of the reason for the provision does not exclude the interpretation adopted by the petitioner. If a husband and wife who own stock jointly are to be treated as a single shareholder even though one of them also owns stock individually, there is no reason to believe that the same rule should not apply when both of them also own stock individually. Nor was the petitioner unreasonable in reading the third sentence of the regulations not to apply in this situation. Although it may be suggested that the regulations deal with joint ownership and therefore the petitioner should have realized that the third sentence implicitly applied to a situation in which the spouses owned stock

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jointly, such a meaning is not expressed, and the implication is not compelling.

The circumstances of this case present an unusual situation. Under the tax laws, the petitioner and its shareholders had the option of having the corporation taxed as an ordinary corporation or electing to have it taxed as a small business corporation. They wished to qualify for the small business corporation treatment, and to achieve that objective, they adopted an interpretation of the regulations which was within the realm of reason and took the action necessary to qualify the corporation for the small business corporation treatment. Had the regulations indicated clearly that in the view of the I.R.S., a husband and wife, both of whom owned stock individually as well as the stock which they owned jointly, would be treated as 2 shareholders, the shareholders of Hicks might have taken different action. For example, they might have transferred sufficient stock into joint ownership to eliminate completely one of the spouses as a separate owner. If we were to adopt the interpretation urged by the respondent, it would now be impossible for the Hicks' shareholders to go back and take the action which would qualify the corporation for the years 1964 through 1967. Thus, in this situation, the petitioner and

its shareholders had a choice to make, and they made it on the basis of a reasonable interpretation of the regulations. For us now to adopt a more restrictive interpretation of those regulations would impose upon them an irreparable detriment. Zellerbach Co. v. Helvering, 293 U.S. 172 (1934); Kean v. Commissioner, 469 F. 2d 1183 (C.A. 9, 1972), affg. in part 51 T.C. 337 (1968), rehearing denied; Columbia Iron & Metal Co., 61 T.C. 5 (1973). Although the shareholders took only the minimum action necessary to qualify the corporation in accordance with their interpretation of the regulations, that fact does not alter our conclusion. Surely, the interpretation of the regulations would not vary whether the spouses individually owned 1 share or 40 shares, in addition to their joint ownership.

In our judgment, the more restrictive interpretation of the regulations now urged by the respondent should not be applied retroactively to invalidate the action taken by the petitioner and its shareholders. Haggar Co. v. Helvering, 308 U.S. 389 (1940); J. C. Penney Co., 37 T.C. 1013 (1962), affd. 312 F. 2d 65 (C.A. 2, 1962). Accordingly, we hold that Mr. and Mrs. Hicks were a single shareholder, that Mr. and Mrs. Emory were a single shareholder, and that the election made by the petitioner in 1964 was

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valid. In reaching that conclusion, we are not passing on what interpretations of section 1371(c) might reasonably be adopted and applied to future transactions.

Although the election was valid when made, the question of its continuing effectiveness in 1966 and subsequent years must also be considered. When Mr. Emory died in 1966, and his estate thereby acquired his shares, it became a new shareholder of the petitioner. Under section 1372 (e) (1), unless a new shareholder files a timely consent to the corporation's election, the election terminates. Section 1.1372-3(b) of the regulations states that the new shareholder's consent must be filed within 30 days after the executor of the estate is qualified as such. Mrs. Emory qualified as executrix of the estate on April 5, 1966, but did not attempt to file the estate's consent until 1972. However, section 1.1372-3(c) of the regulations allows the respondent to grant an extension of time for consents to be filed in certain cases. In this case, the respondent granted an extension of time to file the consent but subsequently attempted to revoke such extension. The petitioner contends that the respondent acted arbitrarily in revoking the extension and that therefore the revocation was ineffective.

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The respondent has maintained that the Tax Court does not have jurisdiction to review the revocation because it does not have equitable powers--its jurisdiction extending only to redeterminations of deficiencies. Secs. 7442, 6214. However, in order to determine tax liabilities, all factors which bear on the matter must be considered. Ben Perlmutter, 44 T.C. 382 (1965), affd. 373 F. 2d 45 (C.A. 10, 1967). In Holmes & Janes, Inc., 30 B.T.A. 74 (1934), the issue presented was the effectiveness of a closing agreement. The respondent had revoked his consent to the agreement because of alleged fraud committed by the taxpayer in drawing up the agreement. He maintained that his action could not be reviewed as it was discretionary with him. In ruling that it did have such power, the Board stated that the "deficiency notice establishes the jurisdiction of the Board to hear and determine all the issues joined in an appeal therefrom." 30 B.T.A. at 79. Here, we must decide whether the petitioner qualifies as a small business corporation, and in order to make that decision, we must decide whether the consents filed in 1972 were valid.

Although the respondent made several general statements as to his reason for revoking the extension, such as needing additional time to consider the matter, the

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only specific reason given for the revocation was that in accordance with his interpretation of the law, an extension to file the consent cannot be granted unless an election to be treated as a small business corporation is then in effect. He suggests that because of his determination that the election was invalid, he should not have granted the extension. He urges that the proper procedure to be followed in this case is for the petitioner to wait until the Court has decided whether the election was valid and then present the request for an extension of time to file the consent. In our opinion, the respondent's position is not required by the law and would result in unnecessary and undesirable delay and litigation.

The petitioner had filed an election to be treated as a small business corporation, and both it and its shareholders had filed returns and proceeded on the assumption that the election was in effect for a number of years prior to the requested extension of time to file the consent. There is no apparent reason as to why the requested extension should not be acted upon merely because that election had been challenged and the issue was then pending in the Tax Court. Certainly, it does not follow, as the respondent appears to suggest, that the election is to be

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treated as invalid for all purposes merely because of his determination to that effect.

Moreover, the procedure urged by the respondent would bifurcate the proceedings. In Kean v. Commissioner, 469 F. 2d 1183 (C.A. 9, 1972), the proceedings were so bifurcated. After the court determined that an individual was a shareholder of a corporation for purposes of the election under section 1372, the shareholder then requested an extension of time to file the required consent, and the I.R.S. denied the request on the ground that the court had already acted. The circuit court rejected such position and held that the refusal to grant the extension was arbitrary and void. If the petitioner in this case were required to wait until the completion of the litigation over the validity of the election, it might encounter similar resistance on the part of the I.R.S., and it would then be necessary to have another trial on the reasonableness of the refusal to grant the extension. Such procedures would be contrary to Rule 1(b) of the Tax Court Rules of Practice and Procedure, which provides that cases should be disposed of speedily. Related or alternative propositions which affect the outcome of a case should be heard and ruled on at the same time. Cf. Tribble v. Bruin, 279 F. 2d 424 (C.A. 4, 1960). Consequently, we hold that

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because the reason given by the respondent for his revocation is insufficient, the revocation is not effective and that the estate's consent filed pursuant to the respondent's original grant of an extension of time for such filing is effective to prevent the termination of the election.

Decision will be entered
for the petitioner.

UNITED STATES TAX COURT
WASHINGTON

HICKS NURSERIES, INC.,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Docket No. 1513-70

DECISION

Pursuant to the determination of this Court as set forth in its Findings of Fact and Opinion filed May 6, 1974, it is

ORDERED and DECIDED: That there are no deficiencies in income tax due from the petitioner for the taxable years 1964, 1965, 1966, and 1967.

(Signed) CHARLES R. SIMPSON

Judge

Entered:

ENTERED MAY 6 1974

FORM 1007-2 (1-67) (CARBON ATTACHED VERSION OF FORM 1007)

UNITED STATES TAX COURT

UNITED STATES
TAX COURT
FILED

HIGGS PURCHASES, INC.,

Petitioner-Appellee,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent-Appellant.

1974 AUG 2 PM 3 41

Docket No. 1513-70

NOTICE OF APPEAL

Notice is hereby given that the Commissioner of Internal Revenue hereby appeals to the United States Court of Appeals for the Second Circuit from the decision of this Court entered in the above-captioned proceeding on the sixth day of May, 1974.

At the time petitioner filed its petition with the Tax Court its principal office was in Westbury, New York, thereby establishing venue in the Second Circuit.

Scott B. Crampton

COJ

SCOTT P. CRAMPTON
Assistant Attorney General
Department of Justice
(SPECIAL) ASST. ATTORNEY GENERAL
COJ

MEADE WHITAKER
Chief Counsel
Internal Revenue Service

OF COUNSEL:

DENNIS J. FOX
Director,
Tax Court Litigation Division
EDWARD D. ROBERTSON
Attorney
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, D.C. 20540

ONLY COPY AVAILABLE

CERTIFICATE OF SERVICE

It is hereby certified that service of this appendix has been made on opposing counsel by mailing four copies thereof on this 12th day of December, 1974, in an envelope, with postage prepaid, properly addressed to them as follows:

Robert Anthoine, Esquire
Glenn Coven, Esquire
Winthrop, Stimson, Putnam and Roberts
40 Wall Street
New York, New York 10005

Gilbert E. Andrews/ewh

GILBERT E. ANDREWS
Attorney